

Audit



Report

OFFICE OF THE INSPECTOR GENERAL

CONSUMABLE ITEM TRANSFER, PHASE II,
CASH IMBALANCE ISSUE

Report No. 97-106

March 5, 1997

19991026 064

Department of Defense

DTIC QUALITY INSPECTED 4

DISTRIBUTION STATEMENT A

Approved for Public Release

Distribution Unlimited

AGI00-01-0180

Additional Copies

To obtain additional copies of this report, contact the Secondary Reports Distribution Unit of the Analysis, Planning, and Technical Support Directorate at (703) 604-8937 (DPS 664-8937), or FAX (703) 604-8932.

Suggestions for Audits

To suggest ideas for or to request future audits, contact the Planning and Coordination Branch, Audit Planning and Technical Support Directorate at (703) 604-8939 (DPS 664-8939) or FAX (703) 604-8932. Ideas and requests can also be mailed to:

OAIG-AUD (ATTN: APTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, Virginia 22202-2884

Defense Hotline

To report fraud, waste, or abuse, contact the Defense Hotline by calling (800) 424-9098; by sending an electronic message to Hotline@DODIG.OSD.MIL; or by writing the Defense Hotline, The Pentagon, Washington, D.C. 20301-1900. The identity of each writer and caller is fully protected.

CIT
DBOF
DLA
ICP

Consumable Item Transfer
Defense Business Operations Fund
Defense Logistics Agency
Inventory Control Point



INSPECTOR GENERAL
DEPARTMENT OF DEFENSE
400 ARMY NAVY DRIVE
ARLINGTON, VIRGINIA 22202-2884



Report No. 97-106

March 5, 1997

MEMORANDUM FOR UNDER SECRETARY OF DEFENSE (COMPTROLLER)
DEPUTY UNDER SECRETARY OF DEFENSE
(LOGISTICS)
ASSISTANT SECRETARY OF THE NAVY (FINANCIAL
MANAGEMENT AND COMPTROLLER)
ASSISTANT SECRETARY OF THE AIR FORCE
(FINANCIAL MANAGEMENT AND COMPTROLLER)
AUDITOR GENERAL, DEPARTMENT OF THE ARMY
DIRECTOR, DEFENSE LOGISTICS AGENCY

SUBJECT: Audit of the Consumable Item Transfer, Phase II, Cash Imbalance Issue
(Project No. 6LD-5036)

Introduction

We are providing this report for your information and use. The Deputy Secretary of Defense directed the transfer of the management of consumable items to the Defense Logistics Agency (DLA) in July 1990. The transfer was separated into two phases. The consumable item transfer (CIT), Phase I, completed in November 1995, included routine, less complex spare parts. CIT, phase II, began in January 1996. It includes items classified as design unstable, have unique end item and critical applications, or require intensive management. In phase II, approximately 148,000 items are scheduled to be transferred by October 1997. However, the Military Departments have threatened to stop the phase II transfer unless DLA agrees to compensate the Military Departments' Supply Management business areas of their Defense Business Operations Fund (DBOF) \$540.5 million for the estimated lost sales revenue from phase II items. As a result of the Military Departments' concern over lost revenues from CIT, phase II, the Under Secretary of Defense (Comptroller), Deputy Comptroller (Program and Budget), issued Program Budget Decision No. 425, which showed the potential cash impacts, estimated by the Military Departments, for their Supply Management business areas of the DBOF to be \$146.4 million for FY 1996 and \$394.1 million for FY 1997. Because the Military Departments' estimates appeared high and varied significantly among the Military Departments, the Deputy Comptroller requested the Inspector General, DoD, to audit the cash impact, the causes for the impact, and the estimated amounts by fiscal year on the Military Departments' Supply Management business areas of the DBOF that may have been caused by CIT, phase II.

Audit Results

Each Military Department computed cash reimbursement estimates differently. The estimates were based on projected lost sales revenue, anticipated disbursements on vendor deliveries for outstanding orders for phase II items, or

a combination of lost sales revenue and disbursements. DLA devised a method that used the net of actual sales of phase II items and the related obligations to replenish inventory to determine amounts to be reimbursed. Our review showed that the Military Departments' estimates were based on past sales histories and that the DLA methodology was the most accurate and consistent way in determining the cash reimbursements due the Military Departments. DLA calculated the reimbursement amount at \$66.5 million, about \$80 million less than the Military Departments estimate (see Enclosure 2). For FY 1997, the DLA methodology should continue to be used to determine the amounts of cash reimbursements due the Military Departments from CIT, phase II items.

Audit Objectives

The audit objectives were to report on the cash impact of the CIT, phase II, during FYs 1996 and 1997 on the Army, Navy, Air Force, and DLA Supply Management business areas of the DBOF, determine whether the Military Departments followed DoD procedures to ensure an orderly transfer of item management responsibility for phase II consumable items to DLA, and whether DLA complied with DoD guidance and applicable regulations. We also included a review of the management control program as it applied to the audit objectives. This report covered the objective to report on the cash impact of the CIT, phase II. We will cover the remaining objectives during the CIT, phase II management portion of the audit under Project No. 6LD-5036.01.

Scope and Methodology

Scope. We reviewed the processes that DLA and the Military Departments used to compute the estimated cash reimbursement amounts to be given to the Military Departments as a result of CIT, phase II. We reviewed accounting reports and item transaction history reports for FY 1996. We reviewed procedures that DLA and the Military Departments used to gather FY 1996 sales and obligations data for CIT, phase II items. We also reviewed procedures used to compute the cash reimbursement amounts for the Military Departments' DBOF Supply Management business areas. Finally, we interviewed Military Department personnel to discuss the methodology they used to arrive at the \$540.5 million cash imbalance.

Methodology. We reviewed FY 1996 sales and obligations data for a judgmental sample, stratified by Military Department, of 300 CIT, phase II items that had been transferred to DLA as of September 15, 1996. Our sample was selected from a universe of 47,413 items and included those items that had the highest demand values for the 12 months preceding the transfer to DLA. The 300 sampled items represented \$145.7 million of the \$274 million in annual demand value that was attributable to the universe of 47,413 CIT, phase II items. We compared the actual sales and obligations data that were recorded at four DLA inventory control points (ICPs) (Defense Electronics Supply Center, Dayton, Ohio; Defense Industrial Supply Center, Philadelphia, Pennsylvania;

Defense Supply Center Columbus, Columbus, Ohio; and the Defense Supply Center Richmond, Richmond, Virginia) to similar data that the DLA Comptroller accumulated in an effort to determine amounts to be reimbursed to the Military Departments as a result of CIT, phase II.

Audit Period and Standards. We performed this economy and efficiency audit from May through October 1996 in accordance with auditing standards issued by the Comptroller General of the United States, as implemented by the Inspector General, DoD.

Contacts During the Audit. We visited or contacted individuals and organizations within DoD. Further details are available on request.

Management Control Program

DoD Directive 5010.38, "Internal Management Control Program," April 14, 1987*, requires DoD managers to implement a comprehensive system of management controls that provides reasonable assurance that programs are operating as intended and evaluate the adequacy of those controls.

Scope of Review of the Management Control Program. We reviewed management controls over the CIT, phase II as they related to the methodology used by DLA and the Military Departments to determine the cash reimbursement amounts for the Military Departments' Supply Management business areas of the DBOF.

Adequacy of Management Controls. Management controls applicable to the objective were deemed to be adequate in that we did not identify any material management control weaknesses.

Prior Audit

Inspector General, DoD, Report No. 94-071, "Transfer of the Management of Consumable Items to the Defense Logistics Agency," March 31, 1994. The report stated that the CIT, phase I program was generally effective. However, there was an inadequate baseline of consumable items to be transferred; filter criteria used to identify items for transfer were revised and not consistently applied at the losing ICPs; DoD procedures for making logistics reassignments were not fully complied with, some essential logistics data were not transferred from the Military Departments to DLA; and no methodology to incorporate program requirements data into the transfer process was established, impacting on weapons systems support programs. The report recommended that the Military Departments follow the prescribed DoD criteria in reviewing

*DoD Directive 5010.38 has been revised as "Management Control Program," August 26, 1996. The audit was performed under the April 1987 version of the Directive.

consumable items for transfer. The report also recommended that staffing levels at DoD ICPs be reviewed, communication and recording of essential logistics data for transferred items be improved, and controls be implemented to ensure that DLA inventory managers use the data. DLA and the Military Departments generally concurred with our recommendations and planned or took actions to satisfy the intent of our recommendations.

Audit Background

DoD Guidance. DoD Manual 4140.26-M, "Integrated Materiel Management of Consumable Items," January 1992, provides policy and establishes uniform guidance and procedures over the management of consumable items. Consumable items are those items for which repair is not economically feasible. Of the 4.1 million consumable items managed in the DoD supply system as of December 1989, 2.9 million items were managed by DLA ICPs and the remaining 1.2 million items were managed by Army, Navy, Air Force, and Marine Corps ICPs.

Consumable Item Transfer. In response to Deputy Secretary of Defense direction, the DLA and the Military Departments developed a plan for the transfer of management, technical, and supply data for consumable items in monthly increments. Phase I was completed in November 1995 with about 760,000 items transferred to DLA. In November 1994, DLA, the designated DoD executive agent for CIT, phase II, issued a memorandum establishing the business rules for CIT phase II. The rules were to be used in conjunction with DoD Manual 4140.26-M. They provided that the inventory of transferred items be given to the gaining DLA ICPs without reimbursement to the losing Military Department ICPs and that outstanding orders for transferred items be paid by the Military Department ICPs. As of April 1996, the phase II baseline was estimated at 148,000 items, about 100,000 less than estimated in March 1995. Upon completion of the CIT, the Military Departments will retain management of about 200,000 consumable items.

Cash Imbalance Issue. In November 1995, the Military Departments, concerned over the amount of anticipated lost sales revenues from CIT, phase II items, informed the Deputy Under Secretary of Defense (Logistics) and the Director, DLA, that they would stop the phase II transfer indefinitely, pending a suitable resolution of the DBOF cash implications of the phase II transfer. In DoD, there is a general agreement that the gaining DLA ICPs experience a cash benefit from the sales of the additional items managed as a result of the CIT. Conversely, the losing Military Departments ICPs incur a related reduction in cash from the loss of sales from items transferred. In the CIT process, the losing Military Department does without sales collections after items are transferred but continues to make disbursements for items on order at the time of transfer. To avoid reduced operations and readiness in the Military Departments, and to ensure a cash neutrality with the CIT, phase II, the Deputy Comptroller requested the Military Departments to submit estimates of the cash impact of CIT, phase II using the general guidance provided.

Discussion

Methodology for Computing Cash Reimbursements. Because the Deputy Comptroller provided general guidance for deriving the estimated cash imbalance impact of the CIT, phase II, each of the Military Departments computed the cash reimbursement amount differently. The delay in transferring CIT, phase II items by the Military Departments also affected the validity of the cash reimbursement estimates. DLA developed a methodology to obtain the actual cash impact of the CIT, phase II.

Military Department Estimates. Each Military Department interpreted the Deputy Comptroller's request differently. The Army's calculation of the cash impact considered the net loss of cash as a result of disbursements for CIT, phase II items on order at the time of transfer. The Navy's calculation considered only lost sales. The Air Force's calculation of the cash impact used the value of lost sales and included disbursements for CIT, phase II items on order at the time of transfer (see Enclosure 3).

Impact of Delayed Transfers. The delayed phase II transfers affected the validity of the cash reimbursement estimates. As of September 1996, 33 percent of the scheduled transfers had not been made. That is, of the scheduled 80,994 items to be transferred, about 54,000 items had been transferred. The Military Departments ranged from 49 percent behind schedule for the Army to 24 percent for the Navy (see Enclosure 1). The cash reimbursement estimates were affected because a prime factor that the Military Departments used for estimating the cash impact of the CIT and the timing of the cash reimbursements to the Military Departments was the number of items to be transferred. The reimbursements would be delayed if the transfer was behind schedule and the overall cash reimbursements would be lower if the number of items transferred was reduced.

DLA Methodology. The DLA devised a methodology to obtain the actual cash impact of CIT, phase II. The DLA method used actual sales of phase II items and obligations to replenish inventory to determine the amount of reimbursement (see Enclosure 3).

Audit Verification of DLA Calculations. Based on the September 30, 1996, sales and obligations amounts that DLA accumulated, reimbursement to the Military Departments for FY 1996 would total about \$66.5 million, which is the net amount of \$78.8 million in sales less \$12.3 million in obligations. The DLA amounts are supported by individual sales and obligations for each item transferred. The sales data can be tracked to actual document numbers for requisitions customers submitted to DLA ICPs. The obligations data can be tracked to the contracts awarded by DLA to replenish inventory. DLA plans to continue to accumulate sales and obligations data on a monthly basis to determine the reimbursement amounts for FY 1997.

To verify the accuracy of the DLA reimbursement amount, we reviewed the sales and obligations data, for a judgmental sample, stratified by Military Department, of 300 CIT, phase II items, that were accumulated in the DLA

Standard Automated Materiel Management System at four DLA ICPs. We reviewed about \$23.4 million (30 percent of \$78 million) in sales revenues and about \$658,000 (5 percent of \$12 million) in contractual obligations that the four DLA ICPs incurred during FY 1996. The actual sales amounts recorded by the DLA ICPs agreed with the sales and obligations amounts recorded by the DLA Comptroller for 295 of 300 items reviewed. We verified that \$23.4 million of the \$23.8 million in actual sales, agreed with the amounts recorded by the DLA Comptroller. For 295 items reviewed, the sales amounts agreed. Records were not available to verify five items with sales of about \$400,000. Our test of 300 items included 7 items with obligations valued at about \$658,000. We verified that the \$658,000 agreed with the amount recorded by the DLA Comptroller.

Impact of Cash Shortage on Military Department Operations. We queried the Military Departments' representatives concerning the impact that would be incurred by each Military Department if the CIT, phase II cash reimbursement was not received. The representatives could not identify the impact to a specific field unit or element but stated that the DBOF surcharge rates, for supplies ordered from the Military Departments' ICPs, and the overhead rates that the Military Departments' depot repair facilities charged, would increase in FYs 1998 and 1999. We could not validate the Military Departments' statements regarding the cash shortage impact.

Conclusion. The method and data that DLA used to estimate the reimbursement amounts for CIT, phase II items were the most objective. In addition, we have no reason to believe that the \$66.5 million reimbursement amount that DLA calculated for items transferred in FY 1996 was incorrect. Also, we concluded that the DLA method in determining cash reimbursement amounts should continue to be used for the remainder of CIT, phase II.

Management Comments and Audit Response

Although no comments were required, the Army, the Navy and the Air Force responded to our draft report. However, the Army did not respond to the draft report in time to have their comments incorporated into the final report. Therefore, the Army comments will be considered as comments to the final report unless additional comments are received. The full text of the Navy and the Air Force comments are in Enclosures 4 and 5, respectively.

Navy Comments. The Navy stated that our report confused two issues, estimating future reimbursements during budget formulation and determining the amount to be transferred during budget execution years. It also stated that there were serious flaws in the DLA methodology for either purpose. The Navy agreed with using actual sales as the basis for determining reimbursement amounts during a budget execution year. However, it stated that the reimbursement amounts could not be used for more than 1 year in advance to prepare budget estimates and that the Navy would need something other than the DLA method for estimating reimbursements when preparing fiscal years 1999 and subsequent budgets. The Navy's most serious concern over using the DLA method for determining the actual reimbursement for fiscal year 1997 was that

DLA subtracted out amounts for new obligations incurred by DLA for inventory replenishments. The Navy believed that this could provide for an unjustified windfall for DLA. Further, the Navy expressed surprise that we could not validate the Navy cash shortage from the CIT, phase II because the Navy's cash shortage was well documented. Finally, the Navy stated that the Navy's estimated sales figures did not incorporate an adjustment for pipeline shortages because, following OSD guidance, the Navy had fully funded the projected sales pipeline so that no adjustment was required, and that estimates made for use during the FY 1998 budget cycle did account for delays in the CIT, phase II transfer process.

Air Force Comments. The Air Force nonconcurred with the report results that DLA reimburse the Air Force \$27.5 million for fiscal year 1996 instead of the \$51.7 million originally requested by the Air Force. The Air Force disagreed with the logic used in the report stating that the report addressed only the cash impact on DLA. The Air Force believed that the audit assessment should have included an evaluation of the cash impact on the Military Departments because the Military Departments make outlays for deliveries of CIT, phase II items for which no sales dollars are captured. The Air Force stated that the audit conclusions could not meet the intention of Program Budget Decision 425 without including the Military Departments' outlays for CIT, phase II item deliveries. The Air Force requested that the audit be reaccomplished in accordance with Under Secretary of Defense (Comptroller), Deputy Comptroller (Program and Budget) guidance and that the Military Departments be given the opportunity to validate the audit methodology.

Audit Response. The audit was requested because the Military Departments used three different methodologies for estimating the CIT, phase II reimbursement amounts and because the Deputy Comptroller (Program and Budget) believed that the estimates were high. We confirmed that the Army and the Air Force estimates were high and that the Navy estimate was low. DLA sales figures were lower than the Army and the Air Force estimates mainly because fewer items were transferred than planned. The Navy estimate was low because the estimate was based on a planned transfer of about 4,500 items; however, the Navy transferred about 12,000 items during fiscal year 1996. We considered sales revenues as the best method for determining cash reimbursement amounts because no matter how much inventory the Military Departments transferred to DLA, cash would be realized only if the inventory sold. No cash would be realized from inactive inventory.

Regarding the Navy comments, the report does not mention nor was there any intention to consider the effects that CIT, phase II would have on fiscal years 1999 and out year budgets. As stated in the audit objectives, we were requested to evaluate the CIT, phase II cash impact on fiscal years 1996 and 1997. The amounts DLA subtracted from sales for obligations from inventory replenishments were subtracted to account for pipeline shortages, and not for the intention of gaining a cash windfall. We did not state that we could not validate that the Navy had a significant cash shortage that would be exacerbated if the Navy was not reimbursed for the CIT, phase II. We stated that the Navy representatives could not identify the cash impact to a specific field unit or

element, and that the Navy representatives stated that the DBOF surcharge rates, for supplies ordered from the Military Departments' ICPs, and the overhead rates that the Military Departments' depot repair facilities charged, would increase in FYs 1998 and 1999. We further stated that we could not validate the Navy representatives statements regarding the cash shortage impact. The Navy's comment on fully funded pipelines is noted. However, because DLA could not identify pipeline shortages to individual line items transferred, obligations incurred by DLA were not subtracted item by item. Instead, to account for total pipeline shortages, the obligations incurred by DLA were prorated to each Military Department based on the percentage of sales experienced for items that each Military Department transferred. Finally, we cannot comment on the Navy's FY 1998 estimates because the FY 1998 estimates were not included in our audit.

The Air Force comments are noted, but we see no need to redo the audit. We disagree that cash outlays by the Military Departments, for inventory delivered to DLA after items had been transferred, must be considered to meet the requirement for cash neutrality. Before DLA can realize cash, the inventory transferred by the Military Departments first must sell. As stated earlier, we confirmed that the cash reimbursement estimates made by the Military Departments were inaccurate, and that the DLA methodology, using actual sales and obligations figures, was the most accurate method used in determining the reimbursement amounts for the Military Departments. We believe that our audit fully satisfied the request of the Deputy Comptroller (Program and Budget). The Air Force is welcome to review our methodology. Arrangements for such a review can be made through the Audit Project Manager.

We appreciate the courtesies extended to the audit staff. For additional information on this report, please contact Mr. Pat Golden, Audit Project Manager, at (215) 737-3881 (DSN 444-3881). Enclosure 6 lists the report distribution. Audit team members are listed on the inside back cover.



Robert J. Lieberman
Assistant Inspector General
for Auditing

Enclosures

Status of CIT, Phase II

The number of items that the Military Departments transferred under CIT, phase II as of September 30, 1996, was behind schedule by about 33 percent*. Behind schedule transfers would cause cash reimbursements to be delayed.

Items Transferred as of September 30, 1996

<u>Military Department</u>	<u>Transfers</u>		<u>Percent Completed</u>
	<u>Planned</u>	<u>Actual</u>	
Army	19,593	9,914	50.6
Navy	15,300	11,617	75.9
Air Force	<u>46,101</u>	<u>32,512</u>	70.5
Total	80,994	54,043	

*26,951 items (80,994 minus 54,043) or 33 percent, were not transferred as scheduled.

CIT, Phase II Reimbursement Amounts

The CIT, phase II reimbursement amount that DLA calculated for FY 1996 was about \$80 million less than the total amount the Military Departments estimated.

FY 1996 DLA Calculations and Military Department Estimates¹ (millions)

	<u>DLA</u>	<u>Military Department</u>	<u>Difference</u>
Army	\$14.5	\$81.0	\$(66.5)
Navy	24.5 ²	13.7	10.8
Air Force	<u>27.5</u>	<u>51.7</u>	<u>(24.2)</u>
Totals	\$66.5	\$146.4	(\$79.9)

¹For FY 1997, the Army, the Navy, and the Air Force respectively requested \$85 million, \$140 million, and \$169.1 million in reimbursements, for a total of \$394.1 million.

²Includes about \$1.7 million for the Marine Corps.

Cash Reimbursement Methodologies

Army. The Army's original estimated cash impact was \$166 million. Because of flawed figures provided by the Army Aviation and Troop Command, St. Louis, Missouri, the Army's estimate was revised downward to \$137.9 million. The Army used anticipated cash outlays on vendor deliveries for outstanding orders for phase II items as a basis for computing the cash reimbursement amount. Each Army ICP computed its portion of the reimbursement estimate individually, based on general guidance that was provided by the Army Materiel Command.

Navy. The Navy's original estimate of the cash impact was \$153.7 million. The estimate was based on a scheduled item transfer of about 4,500 items for FY 1996. However, the Navy proceeded to transfer about 12,000 items as of September 30, 1996, and revised the estimated cash impact upward to \$181.5 million. The Navy based its reimbursement estimate on projected sales that would be lost for those items that were transferred to DLA. The Navy ICP reviewed each CIT, phase II item to compute projected lost sales. The sales numbers were based on a full pipeline of inventory being transferred with each item. Accordingly, the Navy's projected sales figures did not incorporate adjustments for pipeline shortages.

Air Force. The Air Force estimate of the cash impact was \$220.8 million. The Air Force used both sales and cash outlay in its computation. The computation was performed entirely at the Air Force Materiel Command. The average sales value for all consumable items managed by the Air Force was used to project the value of lost sales for CIT, phase II. The consumable item population used by the Air Force to compute the average sales and cash outlay amounts included consumable items that the Air Force planned to retain as well as those to be transferred to DLA.

DLA. The DLA method tracked actual sales for each CIT, phase II item. Sales were totaled for FY 1996 and the FY 1996 obligations that DLA incurred during FY 1996 to replenish inventory, were subtracted to arrive at the net reimbursement amount. The obligations incurred were not subtracted item by item, but were prorated by Military Department based on the percentage of sales experienced for the Military Department's items transferred.

Department of the Navy Comments



THE ASSISTANT SECRETARY OF THE NAVY
(FINANCIAL MANAGEMENT AND COMPTROLLER)
1000 NAVY PENTAGON
WASHINGTON, D.C. 20350-1000

24 JAN 1997

MEMORANDUM FOR THE DEPARTMENT OF DEFENSE INSPECTOR GENERAL

SUBJECT: Draft Audit of the Consumable Item Transfer, Phase II, Cash Imbalance Issue
(Project No. 6LD-5036)

Your draft audit dated 26 November 1996 concludes that the Defense Logistics Agency (DLA) approach should be used in determining cash reimbursement due to the Services for Phase 2, Consumable Item Transfer (CIT). The draft confuses two issues: estimating future reimbursements during budget formulation and determining the amount to be transferred during an execution year. There are serious flaws in the DLA methodology for either purpose.

You note that the DLA method uses actual sales minus new obligations. While we would agree with using actual sales as the basis for determining reimbursement during a year of execution, they obviously cannot be used more than a year in advance to prepare budget estimates. Thus we will need something other than the DLA method to use in estimating reimbursements during the preparation of FY99 and subsequent budgets. As enclosure 2 shows, the DON underestimated actual sales for FY96. Since the DLA method cannot be used for developing future budgets, it would appear that the DON method would provide a conservative estimate for that purpose.

Our most serious concern is with using the DLA method for determining actual reimbursement for FY97 (or any subsequent year) because it subtracts from the reimbursement due to a Service the new obligations DLA makes to replenish its inventory. DLA will be reimbursed for those expenses when it sells the new material. If DLA projects a cash shortfall because it will have to pay for replacement items before it receives the proceeds of their sale, that is one of the unanticipated consequences of the decision to break up DBOF cash, and the Services should not suffer from it. Subtracting DLA obligations for replacement items from the reimbursement to the Services shortchanges Service cash accounts and provides an unjustified windfall to DLA.

I am surprised by the statement that you could not validate the fact that the DON has a significant DBOF cash shortage and that it would be exacerbated if we are not reimbursed for CIT (bottom of page 6). The cash problem certainly is well documented and the relationship of CIT reimbursement to cash seems self evident. We will be happy to provide any additional information you need.

As a matter of fact, the Navy's estimated sales figures did not incorporate an adjustment for pipeline shortages (enclosure 3) because, following OSD guidance, the Navy had fully funded the projected sales pipeline so that no adjustment was required. Similarly, estimates are revised

Department of the Navy Comments

every budget cycle so that estimates made for use during the FY98 budget cycle did account for delays in the transfer process (page 5).

As a minor point, where you describe DLA rules for phase 2 (page 4), you might note that those rules were promulgated before the decision was made to distribute DBOF cash to the Military Departments, and that it is only the decision to create separate cash accounts that makes reimbursement an issue.

Thank you for the opportunity to comment on the draft report. My point of contact for further information is CDR Michelle McAtee, 703-614-0093, FMB41.



Deborah P. Christie
Assistant Secretary of the Navy
(Financial Management and Comptroller)

cc: Deputy Comptroller, Program/Budget

Department of the Air Force Comments



DEPARTMENT OF THE AIR FORCE
HEADQUARTERS UNITED STATES AIR FORCE
WASHINGTON DC

MEMORANDUM FOR ASSISTANT INSPECTOR GENERAL FOR AUDITING 29 Jan 97
OFFICE OF THE INSPECTOR GENERAL
DEPARTMENT OF DEFENSE

FROM: HQ USAF/IL
1030 Air Force Pentagon
Washington, DC 20330-1030

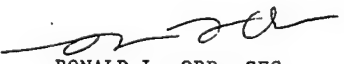
SUBJECT: DoD (IG) Draft Audit of the Consumable Item Transfer, Phase II (CIT PH II), Cash
Imbalance Issue (Project No. 6LD-5036) (SAF/FMPF Memo, 27 Nov 96)

The AF non-concurs with draft audit findings recommending DLA reimburse \$27.5M in FY 96 to the AF vice the \$51.7M originally requested.

The AF disagrees with the fundamental logic used in this audit because it only addresses the cash impact on DLA -- the net of actual sales and related obligations. This is inconsistent with the guidance outlined in PBD 425 which identifies that auditor assistance is required in determining the actual cash impact. In our view, the audit assessment must include an evaluation of the cash impact on the Components. Each Service has made (and continues to make) outlays for transferred CIT PH II items for which no sales dollars are captured. The audit conclusions cannot meet the requirement to be cash neutral (as described in PBD 425) without including Component outlays required by item deliveries.

Request this audit be reaccomplished in accordance with OSD guidance. We also request the Services have the opportunity to validate the methodology used in compiling this audit.

This is a coordinated AF/IL and SAF/FM response.


RONALD L. ORR, SES
Acting, DCS/IL

cc:
SAF/FM
SAF/LLR
AFMC/FMB

Report Distribution

Office of the Secretary of Defense

Under Secretary of Defense (Comptroller)
Deputy Chief Financial Officer
Deputy Comptroller (Program and Budget)
Under Secretary of Defense for Acquisition and Technology
Deputy Under Secretary of Defense (Logistics)
Assistant Deputy Under Secretary of Defense, Materiel and Resource
Management Policy
Director, Defense Logistics Studies Information Exchange
Assistant Secretary of Defense (Public Affairs)

Department of the Army

Deputy Chief of Staff (Logistics)
Commander, Army Materiel Command
Auditor General, Department of the Army

Department of the Navy

Assistant Secretary of the Navy (Financial Management and Comptroller)
Commander, Naval Supply Systems Command
Auditor General, Department of the Navy

Department of the Air Force

Assistant Secretary of the Air Force (Financial Management and Comptroller)
Deputy Chief of Staff (Logistics and Engineering)
Commander, Air Force Materiel Command
Auditor General, Department of the Air Force

Other Defense Organizations

Director, Defense Contract Audit Agency
Director, Defense Logistics Agency
Director National Security Agency
Inspector General, National Security Agency
Inspector General, Defense Intelligence Agency

Non-Defense Federal Organizations and Individuals

Office of Management and Budget
General Accounting Office
National Security and International Affairs Division
Technical Information Center

Chairman and ranking minority member of each of the following congressional committees and subcommittees:

Senate Committee on Appropriations
Senate Subcommittee on Defense, Committee on Appropriations
Senate Committee on Armed Services
Senate Committee on Governmental Affairs
House Committee on Appropriations
House Subcommittee on National Security, Committee on Appropriations
House Committee on Government Reform and Oversight
House Subcommittee on National Security, International Affairs, and Criminal
Justice, Committee on Government Reform and Oversight
House Committee on National Security

Audit Team Members

This report was prepared by the Logistics Support Directorate, Office of the Assistant Inspector General for Auditing, DoD.

Shelton R. Young
Pat Golden
Paul A. Hollister
Herman Tolbert
Alexander L. McKay
Theresa M. Grafenstine
Frank C. Sonsini

INTERNET DOCUMENT INFORMATION FORM

A . Report Title: Consumable Item Transfer, Phase 2, Cash Imbalance Issue

B. DATE Report Downloaded From the Internet: 10/26/99

C. Report's Point of Contact: (Name, Organization, Address, Office Symbol, & Ph #): OAIG-AUD (ATTN: AFTS Audit Suggestions)
Inspector General, Department of Defense
400 Army Navy Drive (Room 801)
Arlington, VA 22202-2884

D. Currently Applicable Classification Level: Unclassified

E. Distribution Statement A: Approved for Public Release

F. The foregoing information was compiled and provided by:
DTIC-OCA, Initials: __VM__ Preparation Date 10/26/99

The foregoing information should exactly correspond to the Title, Report Number, and the Date on the accompanying report document. If there are mismatches, or other questions, contact the above OCA Representative for resolution.